

**DEPARTMENT OF FOOD AND AGRICULTURE**  
**Proposed Changes to Title 3, Chapter 3, Subchapter 1**  
**California Code of Regulations**

**INITIAL STATEMENT OF REASONS**

**Specific Purpose of the Regulation**

The enactment of Senate Bill 1381 (Ch. 164/2000) made significant changes to the provisions which govern dairy marketing practices in the Food and Agricultural Code (FAC). It also required the Department to adopt regulations to establish procedures necessary to determine compliance with the amended law. The purpose of these regulations is to amend and/or repeal existing regulations and adopt new regulations to conform to the revised law.

**Necessity**

The purpose of the Unlawful Practices provisions in the FAC is to state the rules by which dairy products may be promoted and sold from manufacturer to retailer to consumer. The goal of the law is to encourage fair competition and to discourage predatory practices in the marketing of dairy products, with the primary focus on prohibition against selling dairy products below the cost to manufacture and to sell the products. Other prohibited marketing practices remaining in the law include: false or misleading advertising; discrimination in price; false statements or representation; and solicitation, collusion, or joint participation between or among buyers and sellers of dairy products to engage in any of these prohibited practices.

SB 1381 was sponsored by a dairy processing trade organization representing a large number of the dairy processors in California. Its purpose was to lessen restrictions in the way dairy products may be promoted and sold to allow processors and retailers more freedom in the marketing of dairy products, and to amplify the sales below cost provision as the primary tool for enforcing compliance. Included in the new law is the requirement to establish procedures, through administrative regulations, to determine cost.

Prior to the enactment of SB 1381, the Unlawful Practices provisions included numerous sections which were very specific, many of which allowed certain exceptions to the sales below cost provisions. These sections facilitated easier enforcement, as they either specifically prohibited an activity, or allowed it. Costs were determined on a per-unit basis, which made violations easier to detect. The repeal of these sections resulted in a law that is less specific in how compliance will be determined. These proposed regulations will establish cost accounting methods and other necessary procedures the Department will use to evaluate compliance.

Sections 1804, 1806, 1808, 1809, 1831, 1930, 1931, 1932, and 1950 will be amended for consistency with current industry marketing practices, terminology, and clarity.

Section 1811 will be adopted to provide key cost element categories and allocation method guidelines for manufacturers, as well as guidelines for identifying and capturing other costs incurred by manufacturers.

Section 1812 will be adopted to provide guidance for identifying and evaluating costs related to typical activities conducted by wholesale customers.

Section 1850 will be adopted to provide guidance in determining and allocating costs resulting from advertising, incentive and promotion activities conducted by manufacturers and wholesale customers.

Sections 1810, 1851, 1851.1, 1870.1, 1870.2, 1871, 1872, 1873, and 1951 will be repealed, as they are either outdated, unnecessary, or lack current statutory authority.

Article 7 will be repealed, as it will be replaced and improved by the adoption of Section 1812.

#### **Technical, Theoretical, and/or Empirical Study, Reports, or Documents**

The Department relied upon recommendations from outside consultants with expertise in accounting and auditing, and dairy industry representatives, in proposing these regulations.

#### **Reasonable Alternatives to the Regulation and the Reasons for Rejecting Those Alternatives**

No other alternatives were presented to or considered by the Department.

#### **Reasonable Alternatives Identified That Would Lessen Any Adverse Impact on Small Business**

The Department has not identified any alternatives, nor have any alternatives been identified and brought to the attention of the Department that would lessen any adverse impact on small business.

**Evidence Supporting Initial Determination of No Significant Adverse Economic Impact on Business**

The proposed regulation should have no significant adverse economic impact on business, as it is implementing legislation sponsored by dairy businesses to enhance sales of dairy products.